NO. 48982-1-II

COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON

WASHINGTON ATTORNEY GENERAL'S OFFICE,
PUBLIC COUNSEL UNIT,
Appellant,

v.

WASHINGTON UTILITIES AND TRANSPORTATION
COMMISSION, a Washington State Agency,
Respondent,

and

AVISTA CORPORATION, d/b/a AVISTA UTILITIES,
Intervenor/Respondent.

AMENDED AMICUS CURIAE BRIEF OF THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

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I. INTRODUCTION

The Court is presented with matters of fundamental precedential impact, the like of which has not been seen in over three decades, concerning now-common Washington Utilities and Transportation Commission ("UTC" or the "Commission") ratemaking practice. Breaking with decades of its own precedent, the Commission has declared that attrition-based ratemaking is no longer relegated to extraordinary circumstances. In fact, the UTC has announced that the circumstances which purportedly gave rise to the attrition adjustment under review are the "new normal." Administrative Record ("AR") at 725 (Order 05 at ¶ 109).

Washington statute governing the UTC, however, has not changed. Nor has the precedent of the Supreme Court of the State of Washington ("Washington Supreme Court"), which definitively affirms the explicit "used and useful" mandate of RCW 80.04.250—i.e., requiring that any plant in rate base, upon which a regulated utility earns a return on investment, must first be found "used and useful" for service in Washington. Yet, the UTC has knowingly increased rate base via an attrition adjustment that, by plain admission of the adjustment's sponsor, is not associated with any "used and useful" plant for customers.

Likewise, the foundational standard of "arbitrary and capricious" jurisprudence, that an agency must abide by its own rules, has not and will not change. The UTC has violated this standard by implementing a $28.3 million attrition adjustment, despite evidence on record that clearly demonstrates that the Commission's own attrition standard had not been met.

Perhaps most concerning of all, the Commission has violated Washington law and its own rules by misapplying "end results" jurisprudence founded in U.S. Supreme Court precedent. If not struck down by this Court, the Commission's misapplication of "end results" jurisprudence would arrogate unlimited authority to the UTC—thereby allowing utility revenue increases, justified on no other evidence than a raw concern, judgment, or feeling from the Commission. At the very least, as a corollary to the impropriety of decisions justified on a naked "end results" basis, a remand is appropriate to correct UTC miscalculation of the attrition adjustment given to Avista Corporation ("Avista" or the "Company").

II. IDENTITY AND INTEREST OF AMICUS CURIAE

The Industrial Customers of Northwest Utilities ("ICNU") is an incorporated, non-profit association of large industrial electric customers in the Pacific Northwest. For decades, ICNU has routinely represented

some of Avista's largest customers, as well as the largest customers of other Washington electric utilities, in ratemaking proceedings before the UTC. Indeed, as the record demonstrates, ICNU was an active participant in the proceeding now on direct review before the Court, including joint filings made with the appellant, the Washington State Attorney General's Office, Public Counsel Unit ("Public Counsel").

As amicus curiae, ICNU's interest is twofold. First, ICNU members served by Avista will be directly affected by the outcome of this direct review. Resource limitations prevented ICNU's involvement in this direct review until now—most notably, Avista filed its 2016 general rate case ("GRC"), UTC Dockets UE-160228 & UG-160229, on the *same day* that the Commission issued Order 06 to conclude Avista's 2015 GRC. With party process in the 2016 GRC running through January 26, 2017, the day before Public Counsel filed its opening brief with the Court, ICNU had neither the time nor resources to devote to additional Avista processes. However, ICNU can now assist the Court as amicus, bringing ICNU's specific familiarity with Avista's 2015 GRC to light.

Second, the far-reaching precedential impacts of the Court's ultimate determinations will affect ICNU members served by other electric utilities regulated by the Commission. ICNU has been alarmed by material misrepresentation of administrative proceedings by the UTC in

respondent briefing. The long-term precedential implications of the Court's decisions have compelled ICNU, as an initial proponent of many of the critical arguments before the Court, to correct the UTC's misrepresentations. Otherwise, the Court may reach decisions based on a misunderstanding of the legal arguments at issue—and thereby establish inadvertently faulty precedent, affecting ICNU members throughout the state.

ICNU files this revised *amicus* brief to address only the legal issues before the Court, as requested by the Court on May 22, 2017, with an extension of time as granted on July 3, 2017. It is ICNU's intent to discuss only the standards by which the Court should judge the Commission's decision in Avista's 2015 GRC, mentioning facts only to provide necessary context and meaning. ICNU believes that its understanding of the law in this area will provide unique insights to the Court as it proceeds with its consideration of this case.

III. STATEMENT OF THE CASE

ICNU essentially finds Public Counsel to have made a fair statement of the facts and procedure relevant to the issues on review. Opening Br. of Appellant at 6-19. Accordingly, ICNU adopts that statement of the case by reference, with the following additional

statements provided to assist the Court, expanding solely on Public Counsel's explanation of the legal standards relevant in this case.

To begin, ICNU supplements Public Counsel's statement on the UTC's "known and measurable" standard. Opening Br. of Appellant at 8-9. As ICNU noted by extended quotation to a UTC order, issued during the pendency of the proceeding under review, the Commission had repeatedly affirmed the known and measurable standard in the years leading up to Avista's 2015 GRC:

> The known and measurable test requires that an event that causes a change in revenue, expense or rate base must be *known to have occurred* during, or reasonably soon after, the historical 12 months of actual results of operations, and the effect of that event will be in place during the 12-month period when rates will likely be in effect. Furthermore, the *actual amount* of the change must be *measurable*. This means the amount typically cannot be an estimate, a projection, the product of a budget forecast, or some similar exercise of judgment – even informed judgment – concerning future revenue, expense or rate base.

AR. 451 (ICNU Post-Hearing Br. at 16) (emphasis added). The point here is that changes in revenue or rate base, according to the Commission's own standard, must normally or "typically" be tied to an "actual" amount of a real or "known" event that is measurable—not a projection of an event, or even a likely event projection (e.g., one based on "informed judgment"), since there is no "actual amount" that can be known or

measured from such a projection to justify an increase in revenue or rate base.

Next, ICNU expands upon the statement of the UTC attrition standard. Opening Br. of Appellant at 12. A close examination of the Commission's own articulation of the standard is helpful:

> Of all the issues Avista raises and to which the other parties responded in this proceeding, none has more direct bearing on consumer rates than the Company's proposal to include adjustments for attrition …. [A]ttrition occurs when the test-period relationship between rate base, expenses and revenues does not hold under conditions in the rate effective period, such that a utility's expenses or rate base grows more quickly than revenues, *and* a utility would likely have no reasonable opportunity to earn its allowed rate of return. An attrition adjustment is a discrete adjustment to the modified historical test year that the Commission may use *when it determines attrition is present.*

AR. 703-04 (Order 05 at ¶ 47) (emphasis added).

As an initial matter, the crucial import of the attrition question now before the Court is apparent by the UTC's recognition that adjustments for attrition had more bearing upon consumer rates than any other issue that parties raised. Second, the UTC expressly articulates a conjunctive test to determine when "attrition occurs." This is critical because the UTC concludes this order paragraph by articulating a rule for itself—i.e., the Commission "may use" an attrition adjustment "when it determines attrition is present."

In other words, a positive determination that attrition "is" present is a requisite antecedent to any later permissive use of an attrition adjustment. Such a determination must not only be contemporaneous, rather than prospective—namely, the UTC must determine that attrition "is" present, not that attrition "may" or "could" be present—but each element of the conjunctive test must also be met. Notably, this includes the high standard that "a utility would *likely* have *no* reasonable opportunity to earn its allowed rate of return." AR. 703-04 (Order 05 at ¶ 47) (emphasis added). Put differently, the absolute outcome of "no" reasonable opportunity for earnings at an allowed rate of return must not simply be possible, but must be affirmatively shown to be "likely."

ICNU also believes that additional statement on what "*Hope* and *Bluefield* generally stand for" will assist the Court. Opening Br. of Appellant at 15. Again, the UTC's own words are telling, stating that "the Supreme Court in *Hope* determined that the Federal Power Commission (FPC) 'was not bound to the use of *any single formula or combination of formulae* in determining rates.'" AR. 734 (Order 05 at ¶ 132) *citing Fed. Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) (emphasis added). The Commission then quoted directly from *Hope* as follows:

> Under the statutory standard of 'just and reasonable' it is the result reached not *the method employed* which is controlling. It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the [Federal Power] Act is at an end. The fact that *the method employed* to reach that result may contain infirmities is not then important.

AR. 734 (Order 05 at ¶ 132) (emphasis added).

The telling aspect of these quotations is that some methodology, formula, or combination is always presumed in ratemaking. The Commission cites authority that does not attempt to rationalize or justify a pure "end results" or ipse dixit/fiat form of ratemaking, utterly devoid of underlying methodology in *some form*. In fact, while alleging that an end result proposed by Public Counsel or ICNU would not be "appropriate under the standards in *Hope* and *Bluefield*," the UTC claims that its rate setting responsibility "turns not on the particular rate making methodology it selects … but on its outcome, or 'end results.'" AR. 734 (Order 05 at ¶ 132). Thus, while the Commission emphasizes the "end results" of an outcome, there is no claim, even by the UTC, that *Hope* and *Bluefield* stand for the proposition that ratemaking should omit selection of at least some "particular rate making methodology." AR. 734 (Order 05 at ¶ 132).

IV. ARGUMENT

In the following argument sections, pursuant to RAP 10.3(e), ICNU generally seeks to avoid repetition of matters in other briefs. As

noted above, ICNU will address only the legal standards by which the Commission's decision should be judged, drawing from the record as necessary to give meaning to these standards. ICNU does not intend to color the Court's understanding of the facts of this case in its advocacy. Public Counsel has cited and quoted extensively from ICNU testimony and briefing within the agency record, rightly pointing out that the express issues raised by ICNU overwhelmingly belie the UTC's contention that "used and useful" challenges were never properly raised in original proceedings. Reply Br. of Appellant at 1-3.

A. The Commission's Attrition Adjustment Must Meet the "Used and Useful" Requirement

Reduced to the barest level, the statutory issue before the Court was originally expressed by ICNU in agency briefing, via direct quotation from a 2012 UTC order: "RCW 80.04.250 allows the Commission to determine for rate making purposes the value of property 'used and useful for service in this state.'" AR. 452 (ICNU Post-Hearing Br. at 17). Conversely, utility property which is not valued on the basis of being used and useful cannot be included in rates without violating statute. Opening Br. of Appellant at 24-28; Reply Br. of Appellant at 4-5.

At hearing, ICNU expressly cross-examined Staff witness Chris McGuire about whether his proposed attrition adjustment satisfied

Washington's used and useful statutory requirement. In response, Mr. McGuire confirmed that the attrition adjustment under review by the Court has *zero* connection to RCW 80.04.250: "I am not testifying to the used and useful nature of any specific plant beyond July of 2015 …. [A]n attrition allowance is an undistributed increase in revenue. This is not any acceptance of some specific plant addition in the future." TR. 457:5-11 (McGuire). *See also* AR 453 (ICNU Post Hearing Br. at 18). Importantly, Mr. McGuire's attrition study included his projection of the Company's capital spending for the rate effective period that followed issuance of the Commission's final order. TR 440:17-442:4 (McGuire). *See also* AR 723-24.

The relevance of Mr. McGuire's frank admission can hardly be overstated. As the UTC itself declares, "the Commission used a modified version of McGuire's attrition study to calculate Avista's final attrition adjustment." UTC Br. at 24. While the Commission did not include a growth trend for distribution plant, "[a]ll other growth trends were maintained *largely as proposed by Staff*." UTC Br. at 24-25 (emphasis added). Clearly, the attrition adjustment calculated by the UTC was based on Staff witness McGuire's attrition study, which Mr. McGuire himself affirmed to be premised on growth trends not based on "the used and

useful nature of any specific plant beyond July of 2015." TR. 457:5-6 (McGuire).

This Court can logically conclude, based on Mr. McGuire's testimony and the lack of a specific revenue allocation to capital plant in the Commission's order, that the $28.3 million attrition allowance given to Avista was nothing more than "an undistributed increase in revenue," completely unrelated to any "specific plant addition" which might be properly added to rate base under the statutory "used and useful" requirement. TR. 457:5-11 (McGuire).

Here, the Washington Supreme Court's longstanding precedent is worth revisiting: "*Obviously*, an uncompleted utility plant is neither employed for service nor capable of being put to use for service; therefore, such a plant is not 'used and useful' for service as required by RCW 80.04.250." *People's Org. for Wash. Energy Resources v. UTC*, 101 Wn.2d 425, 430 (1984) ("*Power 84*" or "*Power I*") (emphasis added). If the Washington Supreme Court found that *actual* plant—merely on account of being uncompleted—was "obviously" not "used and useful" under RCW 80.04.250, then the UTC's attrition adjustment, as purposely dissociated from *any* specific plant additions, is all the more removed from the used and useful requirements of RCW 80.04.250.

ICNU framed the repercussions of the *Power 84* determination as follows:

> Simply put, the used and useful statute prohibits the … incorporat[ion of] indeterminate future capital amounts into tariff charges, as the Washington Court of Appeals recently recognized when citing to POWER I: "It is beyond cavil that tariffs may not repeal or supersede a statute." The Supreme Court's decision in POWER I is especially relevant to the consideration of the attrition adjustment … given the Commission's recognition "[t]hat the legislature subsequently amended the [used and useful] statute to provide a *specific exception* for CWIP," as a result of POWER I. That is, the legislature authorized just one limited CWIP exception to the Court's holding in POWER I, but made no other modifications to the statute that could be viewed as detracting from the Court's identification of a general statutory prohibition against including "uncompleted utility plant" in rates. Thus, the Company's attrition proposal falls within the general statutory prohibition, since it is founded not on CWIP but on speculative capital expenditure trending (i.e., "uncompleted utility plant").

AR. 452-53 (ICNU Post-Hearing Br. at 17-18) (original emphasis and citations omitted).

In conclusion, the Commission erred by adopting the attrition study performed by Mr. McGuire, without excising capital spending unrelated to the Company's expected distribution plant costs. These forecasted capital costs were placed into rates without allocation to a specific utility facility, and without first having been determined to be "used and useful" as required by RCW 80.04.250. The Commission's

error resulted in rates that included costs for capital facilities that were either not yet in service or had not been determined to be "used and useful." Under either circumstance, the Commission's order violated RCW 80.04.250.

B. The UTC Must Follow its Own Rules, Including its Standard for Granting Attrition Adjustments

Adapting the phrasing of the Court of Appeals, "it is beyond cavil that" agencies must follow their own rules. *See, e.g., Steenholdt v. F.A.A.*, 314 F.3d 633, 639 (D.C. Cir. 2003); *United States ex rel. Accardi v. Shaughnessy*, 347 U.S. 260 (1954). Moreover, an agency that breaks or fails to follow its own rules will be found to have acted in an arbitrary and capricious manner. *Natl. Ass'n of Home Builders v. Norton*, 340 F.3d 835, 852 (9th Cir. 2003).

In the proceeding on review, the UTC acted arbitrarily and capriciously in failing to follow its own rules as to when an attrition adjustment may be applied.

As noted in ICNU's elaboration on the statement of the case, the Commission "may use" an attrition adjustment only when it first determines that "attrition *is* present." AR. 704 (Order 05 at ¶ 47) (emphasis added). Yet, in regard to Avista's electric operations, the record plainly shows that the UTC made no such contemporaneous finding

that attrition "is" present. Quite the opposite, the Commission openly acknowledged that "the record shows that Avista's electric operations are *currently* financially healthy." AR. 733 (Order 05 at ¶ 131) (emphasis added). Further, a determination that "attrition is present" depends upon the satisfaction of the UTC's own conjunctive test, the second element of which is that "a utility would *likely* have *no* reasonable opportunity to earn its allowed rate of return." AR. 703-04 (Order 05 at ¶ 47) (emphasis added).

Specifically, while the record showed Avista to have "actually earned near or above authorized levels for its Washington electric operations for the past two years," the UTC was "concerned this may not hold in the rate year or beyond." AR. 733 (Order 05 at ¶ 131). This concern that good earnings "may not hold" is both a further recognition that attrition was not then present (i.e., a fear that earnings would not "hold") and something far less than an affirmative determination that "no reasonable opportunity" for authorized earnings was "likely" (i.e., the mere concern that a future decline "may" occur).

Likewise, the UTC went on to state: "Absent an attrition adjustment, we are concerned that the Company *may not have an opportunity* to achieve earnings on electric operations at or near authorized levels." AR. 733-34 (Order 05 at ¶ 131) (emphasis added). Needless to

say, the fear that Avista "may not have an opportunity" for authorized earnings is markedly distinct from a definitive finding that Avista was "likely to have no reasonable opportunity" for such earnings. In fact, even the Commission's assertion of concern is undermined by Mr. McGuire's express admission that his attrition study did not consider whether capital plant would actually be constructed in the rate effective period.

In sum, should the Court find that the Commission's statements highlighted by other parties to this case demonstrate that the UTC approved an attrition adjustment in violation of its own standards, then the Commission's actions would be *ipso facto* arbitrary and capricious. Adapting the UTC's own phrasing, this is "Arbitrary and Capricious 101." See UTC Br. at 14.

C. "End Results" Precedent Is Not a License for Fiat Ratemaking

As noted in ICNU's expanded statement of the case, the "end results" jurisprudence attributed to *Hope*, *Bluefield*, and their progeny presupposes the use of at least some underlying methodology to reach "end results." In practice, however, the UTC has misappropriated "end results" precedent to justify an unprincipled ratemaking approach that would allow the Commission to approve any future rate result by mere fiat, divorced from any tether to statute or methodological development.

If not struck down, the UTC's arrogation of power would obviate the relevance of evidentiary ratemaking process. That is, if attrition adjustments and other actions can be justified *despite* evidence showing statutory violations and inconsistency with the Commission's own rules—simply upon a claim that "end results" trump any alleged infirmities—then future Commission process will devolve into an expensive and time-consuming farce. Yet, as the Commission acknowledges (without an apparent appreciation of full precedential import), the Washington Supreme Court referenced the "end results" jurisprudence in *Power 84* and "observed that 'within a fairly broad range, regulatory agencies exercise substantial discretion in selecting the appropriate rate making methodology.'" AR. 734-35 (Order 05 at ¶ 133). First, the recognition of a "range" of discretion, however broad, is also a recognition that "end results" precedent is not a license for unfettered UTC discretion. In other words, *Power 84* inherently affirms the restraints of standards like the used and useful requirement of RCW 80.04.250, which shape the range "within" which the UTC must operate.

Second, the express recognition that discretion is exercised by the selection of "appropriate rate making methodology" necessarily conveys that other, "inappropriate" methodologies exist which the UTC may not use. In this manner, *Power 84* repudiates any notion that the Commission

can simply point to "end results" as a justification for ratemaking action, regardless of methodological infirmities employed.

V. CONCLUSION

For the reasons stated above, in addition to those briefed by Public Counsel, the Court should reverse and remand on all assignments of error.

Dated this 7th day of July, 2017.

Respectfully submitted,

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July 07, 2017 - 11:46 AM

Transmittal Information

Filed with Court:	Court of Appeals Division II
Appellate Court Case Number:	48982-1
Appellate Court Case Title:	Attorney General's Public Counsel Unit, Petitioner v WA Utilities & Transportation Comm Respondents
Superior Court Case Number:	16-2-01108-7

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